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PLR-143400-07

Date:

May 09, 2008

Legend:

Husband	=
Wife	=
Daughter	=
Charity	=

Family Trust	=
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Court	=
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Trustee	=
State Law 1	=
State Law 2	=
State Law 3	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
State	=
<u>X</u>	=
<u>Y</u>	=
<u>Z</u>	=

Dear :

This letter is in response to a letter dated September 24, 2007, and subsequent correspondence, from your authorized representatives requesting rulings under § 2055 of the Internal Revenue Code, with respect to the reformation of two trusts, and under § 2518, with respect to a disclaimer of certain interests in the trusts.

The facts submitted and the representations made are summarized as follows.

The Family Trust

Husband and Wife were married and, prior to their deaths, they executed Family Trust, a revocable trust. Paragraph 3(e)(2) of Family Trust provides that upon the death of the first taxpayer to die, Family Trust is to be divided into three subtrusts, Survivor's Trust, Marital Deduction Trust, and Residual Trust. The provisions of Family Trust govern the three subtrusts.

Sections (a) and (b) of Paragraph 4 of Family Trust provide that during Wife's life, the trustee will pay Wife the net income of Survivor's Trust in quarter-annual or more frequent installments and such amounts of principal as the trustee, in the trustee's discretion, considers necessary for Wife's proper health, support, comfort, enjoyment, and welfare. Paragraph 4(c) provides that during the lifetime of Wife, or upon her death, Wife has the power to appoint principal and any undistributed income of Survivor's Trust to one or more persons or entities, either outright or in trust, as Wife may decide. Such power is exercisable by Wife alone and in all events. Paragraph 4(e) provides that on the death of Wife, and in default of Wife's exercise of any power of appointment, the balance of Survivor's Trust will be added to Residual Trust.

Sections (a) and (b) of Paragraph 5 provide that during Wife's life, the trustee will pay Wife the net income of Marital Deduction Trust in quarter-annual or more frequent installments and such amounts of principal, up to the whole of it, as Wife may direct from time to time. Paragraph 5(c) provides that on the death of Wife, the trustee shall distribute the balance then remaining of Marital Deduction Trust to one or more persons or entities, including Wife's own estate, either outright or in trust, as Wife shall appoint by will. Paragraph 5(d) provides that on the death of Wife, and in default of Wife's exercise of her power of appointment, the balance of Marital Deduction Trust will be added to Residual Trust.

Paragraph 6(a) provides that the trustee will pay $\frac{y}{z}$ of the net income of Residual Trust to Wife and $\frac{z}{y}$ of the net income to Daughter, in quarter annual or more frequent installments. Paragraph 6(c) provides that upon the death of Wife, the trustee will pay $\frac{y}{z}$ of the net income to Daughter and $\frac{z}{y}$ of the net income to Charity. Paragraph 6(d) provides that upon the death of Daughter, the balance of Residual Trust will be distributed to Charity.

Paragraph 6(e) provides that:

The Trustee shall have the right to invade the principal of the Residual Trust for any beneficiary thereof, up to the portion of that beneficiary's income interest, if, in the discretion of the Trustee, the payments from

such trust are insufficient to provide for the proper education, health, maintenance and support of such beneficiary.

Judicial Proceeding to Reform Survivor's Trust and Marital Deduction Trust

Husband died on Date 1. Wife died on Date 2, without exercising any powers of appointment. Upon Husband's death Residual Trust was funded with assets that were included in Husband's gross estate; Survivor's Trust and Marital Deduction Trust were funded with assets that were included in Wife's gross estate. Under Paragraph 6 of Family Trust, Survivor's Trust and Marital Deduction Trust do not qualify as charitable remainder trusts under § 664 and, therefore, Wife's estate is not eligible for a charitable deduction for Charity's interest in Survivor's Trust and Marital Deduction Trust under § 2055(e)(2).

In order to qualify Survivor's Trust and Marital Deduction Trust under § 2055(e)(2) for the estate tax charitable deduction, Daughter, as trustee and an income beneficiary of Survivor's Trust and an income beneficiary of Marital Deduction Trust, petitioned Court to amend Paragraphs 4(e) and 5(d) of Family Trust to provide that upon Wife's death, the balance of Survivor's Trust and Marital Deduction Trust will be distributed to Unitrust, a trust intended to qualify as a charitable remainder unitrust under § 664(d), instead of being distributed to Residual Trust, pursuant to State law and § 2055(e)(3). Daughter initiated this judicial proceeding on Date 3, within 90 days of the due date of Wife's federal estate tax return. This petition was granted by Court in an order on Date 4. The petition stated that Survivor's Trust and Marital Deduction Trust have requested a ruling from the Internal Revenue Service that the proposed modification that was approved by Court will result in allowance of the estate tax charitable deduction. In order to obtain favorable rulings from the Service, Daughter will file an amended petition with Court to further amend Paragraphs 4(e) and 5(d) as follows.

Paragraph 4(e), as amended, provides that:

Upon the death of the [Wife] . . . the Survivor's Trust shall terminate, and the Trustee shall distribute the balance of the Survivor's Trust to the Trustee of the [Unitrust], hereby established, to be administered and distributed in accordance with the provisions set forth hereinbelow. The provisions relating to the Unitrust set forth hereinbelow shall supersede any conflicting provisions of the Survivor's Trust or the Marital Deduction Trust.

. . .

During the lifetime of [Daughter] . . . , the Trustee, during each taxable year (including any short taxable year) of the Unitrust, shall pay, in equal quarterly installments on the last day of each calendar quarter, an amount

(the 'unitrust amount') equal to x percent of the net fair market value of the Unitrust, subject to the other provisions hereof, as follows: (i) to [Daughter]: y of the unitrust amount; and to Charity: z of the unitrust amount. The obligation to pay the unitrust amount begins as of the date of the [Wife's] death

Unitrust shall terminate upon [Daughter's] death. Upon termination, the Trustee shall distribute the Unitrust assets . . . to Charity; provided, however, that if Charity is not an organization described in Code Sections 170(c), 2055(a), and 2522(a) at the time any amount is to be transferred to Charity, that amount instead shall be transferred to Charity's legal successor-in-interest [provided that that organization is then described in those Sections

Paragraph 5(d), as amended, provides:

If and to the extent that the [Wife] shall fail to exercise such power of appointment, the balance remaining in this Marital Deduction Trust . . . shall be distributed [to] the Trustee of the Unitrust established pursuant to the provisions of Paragraph 4(e) hereof, to be administered and distributed in accordance with the provisions set forth in that Paragraph 4(e), which provisions shall supersede any conflicting provisions of the Survivor's Trust or Marital Deduction Trust.

The only beneficiaries of Survivor's Trust and Marital Deduction Trust are Daughter and Charity, both of whom will be given timely notice of the hearing of the amended petition. Trustee of Marital Deduction Trust and Residual Trust and the Attorney General will also be given timely notice of the hearing of the amended petition. Both beneficiaries have consented to the proposed modifications requested in the amended petition.

State Law 1 provides that, "[e]xcept as provided in subdivision (b), if all beneficiaries of an irrevocable trust consent, they may compel modification or termination of the trust upon petition of the court.

In this case, based upon the information provided, the difference between the actuarial value of the qualified interest and the actuarial value of the reformable interest as of Wife's death in Unitrust will not exceed 5 percent of the actuarial value of the reformable interest as of the date of Wife's death.

Daughter's Disclaimer

Within nine months of Decedent's death, Daughter executed a written document in which Daughter disclaimed her interest in discretionary principal distributions from Survivor's Trust and Marital Deduction Trust.

I, [Daughter], hereby disclaim all of my interests in the [Survivor's Trust] and the [Marital Deduction Trust] that are described in Paragraph 6(e) of the [Family Trust] (on page 10 thereof) (to the extent those interests come from the Survivor's Trust and the Marital Deduction Trust.

It has been represented that within nine months of Decedent's death, Daughter delivered the disclaimer to the appropriate parties required under § 2518, and filed the disclaimer with Court, the court where Decedent's estate is being administered. It has been further represented that Daughter has not accepted any interest in the disclaimed property. Finally, it has been represented that, as a result of the disclaimer, Daughter has not retained any means of directing to whom the disclaimed property is to be distributed.

State Law 2 provides, in relevant part, that a disclaimer shall be filed with any of the following: (1) the superior court in the county in which the estate of the decedent is administered; (2) the trustee, personal representative, other fiduciary, or person responsible for distributing the interest to the beneficiary; or (3) any other person having custody or possession of or legal title to the interest.

State Law 3 provides, in relevant part, that unless the creator of the interest provides for a specific disposition of the interest in the event of a disclaimer, the interest disclaimed shall descend, go, be distributed, or continue to be held (1) as to a present interest, as if the disclaimant had predeceased the creator of the interest or (2) as to a future interest, as if the disclaimant had died before the event determining that the taker of the interest had become finally ascertained and the taker's interest indefeasibly vested. A disclaimer relates back for all purposes to the date of the death of the creator of the disclaimed interest or the determinative event, as the case may be.

The executrix is requesting the following rulings:

1. Daughter's disclaimer of her interest in discretionary principal distributions from Survivor's Trust and Marital Deduction Trust is a qualified disclaimer under § 2518.
2. The proposed reformation of Survivor's Trust and Marital Deduction Trust will be a qualified reformation under § 2055(e)(3).
3. An estate tax charitable deduction is allowable to Wife's estate under § 2055(a) for the actuarial date of death value of Charity's income and remainder interest in Unitrust.

Ruling 1

Section 2046 provides that, for estate tax purposes, disclaimers of property interests passing upon death are treated as provided in § 2518.

Section 2518(a) provides that, if a person makes a qualified disclaimer of an interest in property, the estate, gift, and generation-skipping transfer tax provisions will apply to that interest as if it had never been transferred to such person.

Under § 2518(b), the term "qualified disclaimer" means an irrevocable and unqualified refusal by a person to accept an interest in property, provided: (1) the disclaimer is in writing; (2) the disclaimer is received by the transferor of the interest, his legal representative, or the holder of legal title to the property, not later than the date which is nine months after the later of the date on which the transfer creating the interest is made or the date on which the person refusing the interest attains age 21; (3) the person disclaiming the interest has not accepted the interest or any of its benefits; and (4) as a result of the disclaimer, the interest passes without any direction by the person making the disclaimer and passes either to the spouse of the decedent or to a person other than the person making the disclaimer.

Section 2518(c)(1) provides that a disclaimer with respect to an undivided portion of an interest which meets the requirements of the preceding sentence shall be treated as a qualified disclaimer of such portion of the interest.

Under § 25.2518-1(b) of the Gift Tax Regulations, if a qualified disclaimer is made, the disclaimed property is treated, for federal gift, estate, and generation-skipping transfer tax purposes, as passing directly from the transferor, and not from the disclaimant, to the person entitled to receive the property as a result of the disclaimer.

Section 25.2518-2(b) provides that, in order to qualify as a qualified disclaimer, the disclaimer must be in writing and the writing must identify the interest in property disclaimed and be signed by either the disclaimant or by the disclaimant's legal representative. In addition, § 25.2518-2(c)(1) provides that the written disclaimer must be delivered (to the transferor's legal representative, etc.) no later than the date which is nine months after the date on which the transfer creating the interest in the disclaimant is made.

Under § 25.2518-2(d)(1), a qualified disclaimer cannot be made with respect to an interest in property if the disclaimant has accepted the interest or any of its benefits, expressly or impliedly, prior to making the disclaimer. Under § 25.2518-2(d)(2), if a beneficiary who disclaims an interest in property is also a fiduciary, actions taken by such person in the exercise of fiduciary powers to preserve or maintain the disclaimed property (e.g., directing the harvesting of a crop or maintenance of a home) is not treated as an acceptance of such property.

Section 25.2518-3(a)(1) provides, in relevant part, that if the requirements of this section are met, the disclaimer of all or an undivided portion of any separate interest in property may be a qualified disclaimer even if the disclaimant has another interest in the same property. In general, each interest in property that is separately created by the transferor is treated as a separate interest. For example, if an income interest in securities is bequeathed to A for life, then to B for life, with the remainder interest in such securities bequeathed to A's estate, and if the remaining requirements of § 2518(b) are met, A could make a qualified disclaimer of either the income interest or the remainder, or an undivided portion of either interest. A could not, however, make a qualified disclaimer of the income interest for a certain number of years.

In Example 5 of § 25.2518-3(d), E died on September 13, 1978. Under the provisions of E's will, E's shares of stock in X, Y, and Z corporations were to be transferred to a trust. The trust provides that all income is to be distributed currently to F and G in equal parts until F attains the age of 45 years. At that time the corpus of the trust is to be divided equally between F and G. F disclaimed the income arising from the shares of X stock. G disclaimed 20 percent of G's interest in the trust. F's disclaimer is not a qualified disclaimer because the X stock remains in the trust. If the remaining requirements of § 2518(b) are met, G's disclaimer is a qualified disclaimer.

In Example 8 of § 25.2518-3(d), assume the same facts as in Example 5 except that F disclaimed the entire income interest in the trust while retaining the interest F has in corpus. Alternatively, assume that G disclaimed G's entire corpus interest while retaining G's interest in the income from the trust. If the remaining requirements of § 2518(b) are met, either disclaimer will be a qualified disclaimer.

In Example 9 of § 25.2518-3(d), G creates an irrevocable trust on May 13, 1980, with H, I, and J as the income beneficiaries. In addition, H, who is the trustee, holds the power to invade corpus for H's health, maintenance, support, and happiness and a testamentary power of appointment over the corpus. In the absence of the exercise of the power of appointment, the property passes to I and J in equal shares. H disclaimed the power to invade corpus for H's health, maintenance, support, and happiness. Because H retained the testamentary power to appoint the property in the corpus, H's disclaimer is not a qualified disclaimer. If H also disclaimed the testamentary power of appointment, H's disclaimer would have been a qualified disclaimer.

In Example 11 of § 25.2518-3(d), under H's will, a trust is created from which W is to receive all of the income for life. The trustee has the power to invade the trust corpus for the support or maintenance of D during the life of W. The trust is to terminate at W's death, at which time the trust property is to be distributed to D. D makes a timely disclaimer of the right to corpus during W's lifetime, but does not disclaim the remainder interest. D's disclaimer is a qualified disclaimer assuming the remaining requirements of § 2518 are met.

In this case, within nine months of Wife's death, Daughter executed a written document in which she disclaimed her interest in discretionary principal distributions to provide for her education, health, maintenance, and support from Survivor's Trust and Marital Deduction Trust. Under State Law 2, Daughter's disclaimer relates back for all purposes to the date of Wife's death.

It has been represented that Daughter has not accepted any interest in the disclaimed property. It has further been represented that within nine months of Wife's death, Daughter delivered the disclaimer to the appropriate parties required under § 2518; and filed the disclaimer with Court, the court where Wife's estate is being administered. Finally, it has been represented that, as a result of the disclaimer, Daughter has not retained any means of directing to whom the disclaimed property is to be distributed.

Accordingly, based upon the facts submitted and the representations made, we conclude that Daughter's disclaimer of her interest in discretionary principal distributions from Survivor's Trust and Marital Deduction Trust is a qualified disclaimer under § 2518.

Ruling 2

Section 664(d)(2) provides that a charitable remainder unitrust is a trust (A) from which a fixed percentage (which is not less than 5 percent nor more than 50 percent) of the net fair market value of its assets, valued annually, is to be paid, not less often than annually, to one or more persons (at least one of which is not an organization described in § 170(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals, (B) from which no amount other than the payments described in § 664(d)(2)(A) and other than qualified gratuitous transfers described in § 664(d)(2)(C) may be paid to or for the use of any person other than an organization described in § 170(c), (C) following the termination of the payments described in § 664(d)(2)(A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in § 170(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in § 644(g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined by § 664(g)), and (D) with respect to each contribution of property to the trust, the value (determined under § 7520), of such remainder interest in such property is at least 10 percent of the net fair market value of such property as of the date such property is contributed to the trust.

Section 2055(a) provides that, for purposes of the federal estate tax, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, and transfers to or for the use of charitable, religious, scientific, literary, or educational organizations described in § 2055(a)(1) through § 2055(a)(4).

Section 2055(e)(2) provides that where an interest in property (other than an interest described in § 170(f)(3)(B)) passes or has passed from the decedent to a person, or for a use, described in § 2055(a), and an interest (other than an interest which is extinguished upon the decedent's death) in the same property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to a person, or for a use, not described in § 2055(a), no deduction shall be allowed under § 2055 for the interest that passes or has passed to the person, or for a use, described in § 2055(a), unless -- (A) in the case of a remainder interest, such interest is in a trust which is a charitable remainder annuity trust or a charitable remainder unitrust (described in § 664) or a pooled income fund (described in § 642(c)(5)), or (B) in the case of any other interest, such interest is in the form of a guaranteed annuity or is a fixed percentage distributed yearly of the fair market value of the property (to be determined yearly).

Section 2055(e)(3) provides for the reformation of interests to comply with the requirements of § 2055(e)(2). Section 2055(e)(3)(A) provides that a deduction shall be allowed under § 2055(a) in respect of any qualified reformation.

Section 2055(e)(3)(B) defines the term "qualified reformation" to mean a change of a governing instrument by reformation, amendment, construction, or otherwise that changes a reformable interest into a qualified interest but only if -- (i) any difference between (I) the actuarial value (determined as of the date of the decedent's death) of the qualified interest, and (II) the actuarial value (as so determined) of the reformable interest, does not exceed 5 percent of the actuarial value (as so determined) of the reformable interest, (ii) in the case of (I) a charitable remainder interest, the nonremainder interest (before and after the qualified reformation) terminated at the same time, or (II) any other interest, the reformable interest and the qualified interest are for the same period, and (iii) the change is effective as of the date of the decedent's death.

Section 2055(e)(3)(C)(i) defines the term "reformable interest" to mean any interest for which a deduction would be allowable under § 2055(a) at the time of the decedent's death but for § 2055(e)(2).

Section 2055(e)(3)(C)(ii) provides that the term "reformable interest" does not include any interest unless, before the remainder vests in possession, all payments to persons other than an organization described in § 2055(a) are expressed either in specified dollar amounts or a fixed percentage of the fair market value of the property.

Section 2055(e)(3)(iii) provides, in part, that § 2055(e)(3)(C)(ii) does not apply to any interest if not later than 90 days after the last date (including extensions) for filing an estate tax return, if an estate tax return is required to be filed, a judicial proceeding is commenced to change the interest into a qualified interest.

Section 2055(e)(3)(D) defines the term "qualified interest" to mean an interest for which a deduction is allowable under § 2055(a).

Section 20.2055-2(a) of the Estate Tax Regulations provides, in relevant part, that if a trust is created or property is transferred for both a charitable and a private purpose, a deduction may be taken of the value of the charitable beneficial interest only insofar as that interest is presently ascertainable, and hence severable from the noncharitable interest.

Section 20.2055-2(c)(1) provides that, in the case of a bequest, devise, or transfer made by a decedent dying after December 31, 1976, the amount of the bequest, devise or transfer for which a deduction is allowable under § 2055 includes an interest which falls into the bequest, devise or transfer as a result of a qualified disclaimer under § 2518.

Daughter's disclaimer of her right to receive discretionary distributions of principal from Survivor's Trust and Marital Deduction Trust is a qualified disclaimer under § 2518. See, Ruling 1. Thus, for estate tax purposes, the interest is treated as never having passed to Daughter. Further, as a result of the disclaimer, Daughter will be treated under State Law 3 as if she predeceased Wife with respect to the disclaimed interest. Thus, for estate tax purposes, as of the date of Wife's death, Daughter's right to receive income from Survivor's Trust and Marital Deduction Trust is deemed to be the only noncharitable interest in those trusts. Therefore, we conclude that the charitable interest in Survivor's Trust and Marital Deduction Trust prior to reformation would have qualified for an estate tax charitable deduction under § 2055(a), but for the provision of § 2055(e)(2). Accordingly, the first requirement for a qualified reformation under § 2055(e)(3) is satisfied.

The proposed reformation will satisfy the second requirement for a qualified reformation under § 2055(e)(3) since Daughter's interest both before and after the proposed reformation will terminate at the same time (i.e., at Daughter's death). The proposed reformation will satisfy the third requirement because the reformation will be effective as of the date of Wife's death. The fourth requirement is satisfied because, based upon the information provided, the difference between the actuarial value (determined as of the date of Wife's death) of the qualified interest and the actuarial value (as so determined) of the reformable interest does not exceed 5 percent of the actuarial value (as so determined) of the reformable interest.

The proposed reformation will satisfy the fifth requirement under § 2055(e)(3) because, even though Paragraphs 4(e) and 5(d) of Family Trust, do not conform to the requirements for charitable remainder trusts under § 664 as required by § 2055(e)(2)(A), Daughter petitioned Court on Date 3 to modify Paragraphs 4(e) and 5(d) of Family Trust to provide that upon Wife's death the trust estate of Survivor's Trust

and Marital Deduction Trust will be distributed to Unitrust, a trust intended to qualify as a charitable remainder unitrust § 664(d), instead of being distributed to Residual Trust. The judicial proceeding was commenced on Date 3, within 90 days of the date that Wife's federal estate tax return was due.

Accordingly, based on the facts submitted and the representations made, we conclude that the proposed reformation of Survivor's Trust and Marital Deduction Trust, will be a qualified reformation for purposes of § 2055(e)(3); provided that the reformation is effective under local law and Unitrust meets the requirements of a charitable remainder unitrust as described in § 664(d)(2).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Lorraine E. Gardner
Senior Counsel, Branch 4
(Passthroughs & Special Industries)

Enclosures: Copy for § 6110 purposes